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FISCAL IMPACT STATEMENT

LS 6519 | **NOTE PREPARED:** Jan 23, 2006
BILL NUMBER: HB 1294 | **BILL AMENDED:**

SUBJECT: Rental Dwelling Property Tax Deduction.

FIRST AUTHOR: Rep. Hoffman | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X **GENERAL** | **IMPACT:** State & Local
X **DEDICATED**
FEDERAL

Summary of Legislation: This bill establishes a property tax deduction for residential rental property. The bill specifies the deduction percentage for taxes payable in 2007 and 2008. It provides that the deduction for taxes payable after 2008 is based on deduction percentages set by the Department of Local Government Finance (DLGF) based on certain guidelines.

Effective Date: Upon passage.

Explanation of State Expenditures: For property taxes payable in 2009, the DLGF would be required to estimate the tax to assessed value (AV) ratio for rental units and for all dwellings. The DLGF would adjust the rental deduction amount as described in *Explanation of Local Revenues.*

The new deduction for rental property in this proposal would cause tax shifts to all property. Subject to appropriation, these shifts could result in an overall increase of PTRC/Homestead Credit expenses ranging from an estimated $1.2 M to $1.6 M in FY 2007 (partial year). The estimated increase ranges from $3.5 M to $4.9 M per year beginning in FY 2008.

Background: The state pays Property Tax Replacement Credits (PTRC) in the amount of 60% of school general fund levies attributable to all property and 20% of the portion of all operating levies (including the remaining 40% of the school GF levy) that are attributable to real property and non-business personal property. Homestead credits are paid by the state in the amount of 20% of the net property tax due for qualifying funds on owner-occupied residences. The total amount of Property Tax Replacement Credits and Homestead Credits is limited to $2,028.5 M for FY 2007. If the total amount to be distributed exceeds the appropriation, then the distribution is proportionately reduced.

Explanation of State Revenues: The state levies a small tax rate for State Fair and State Forestry. Any reduction in the assessed value base will reduce the property tax revenue for these two funds. The reduction in state revenue under this bill is estimated at between \$86,000 and \$117,000 in FY 2007 and between \$172,000 and \$235,000 per year beginning in FY 2008.

Explanation of Local Expenditures:

Explanation of Local Revenues: Beginning with taxes payable in 2007 under this proposal, each building containing rental property would be eligible for a property tax deduction. The deduction would vary depending on the number of units in a building and would equal the following:

Buildings with less than 5 units: – The lesser of 50% of gross AV or \$23,100 total;
Buildings with 5 to 8 units – The lesser of 50% of gross AV or \$5,775 per unit;
Buildings with 9 to 20 units – The lesser of 50% of gross AV or \$3,465 per unit; and
Buildings with more than 20 units – The lesser of 50% of gross AV or \$2,310 per unit.

According to 2000 Census figures, there were about 187,750 single-unit rentals, 84,900 units in 2-unit buildings, 100,800 units in 3- or 4-unit buildings, 115,300 units in 5- to 9-unit buildings, 81,400 units in 10- to 19-unit buildings, and 104,900 units in buildings containing at least 20 dwellings. These counts provide an estimated total maximum statewide deduction of about \$7.2 B.

An examination of 2003 parcel-level data suggests that the total of all rental deductions could be as high as \$9.8 B. The unit count ranges in this data are not as precise as the census data. This estimate includes all dwellings that are not homesteads, even if they are not rentals (i.e., vacation homes). So, this estimate represents the potential maximum impact of this deduction.

Taking both data sources into consideration, it is estimated that the total rental deduction under this bill would be between \$7.2 B and \$9.8 B.

A reduction of the assessed value base causes a shift of the property tax burden from the taxpayers receiving the deductions to all taxpayers in the form of an increased tax rate. The \$7.2 B to \$9.8 B reduction in AV would cause an estimated 4.1% to 5.7% increase in the statewide average net tax rate, causing a shift to other taxpayers ranging from about \$135 M to \$184 M per year beginning in CY 2007.

Total local revenues, except for cumulative funds, would remain unchanged. The revenue for cumulative funds would be reduced by the product of the fund rate multiplied by the AV reduction amount applicable to that fund.

For taxes payable after 2008, the deduction amount would be adjusted in each year in order to maintain the 2002 ratio of (1) gross tax per \$1 of gross AV for principal rental dwellings to (2) gross tax per \$1 of gross AV for all dwellings. This provision could result in a nominal increase or reduction in the rental dwelling deduction beginning in CY 2009. The deduction amounts allowed in this bill for 2007 and 2008 equal 66% of the homestead standard deduction. As the deduction is increased, the gross tax per \$1 of gross AV declines.

State Agencies Affected: Department of Local Government Finance.

Local Agencies Affected: County and township assessors; County auditors.

Information Sources: Dataset: SF3, Tables: H7 and H30, U.S. Census Bureau; Local Government Database; 2002 and 2003 parcel-level county auditor property tax data.

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